RICHARD RUSSELL'S **DOW THEORY LETTERS, INC.**

P. O. Box 1759, La Jolla, California 92038
Minimum of 26 Letters per year – $185 Annually
Registered with the Securities and Exchange Commission

November 17, 1982 **LETTER 848**

Nov. 5, DJIA 1051.78; PTI 1384; A-D Ratio –19.25
Nov. 12, DJIA 1039.92; PTI 1384; A-D Ratio –19.09

THE MARKET: November 3, 1982 was an historic day on the NYSE. The Averages had turned up from their August 12 bear market lows (Industrials 776.92, Transports 292.12). With only a 7 day decline in September and a 5-day decline during October-November, the Averages roared to all-time highs on November 3. Thus, in the space of only 57 trading days the D-J Averages advanced from bear market lows to all-time highs. Never in stock market history has anything like this been seen.

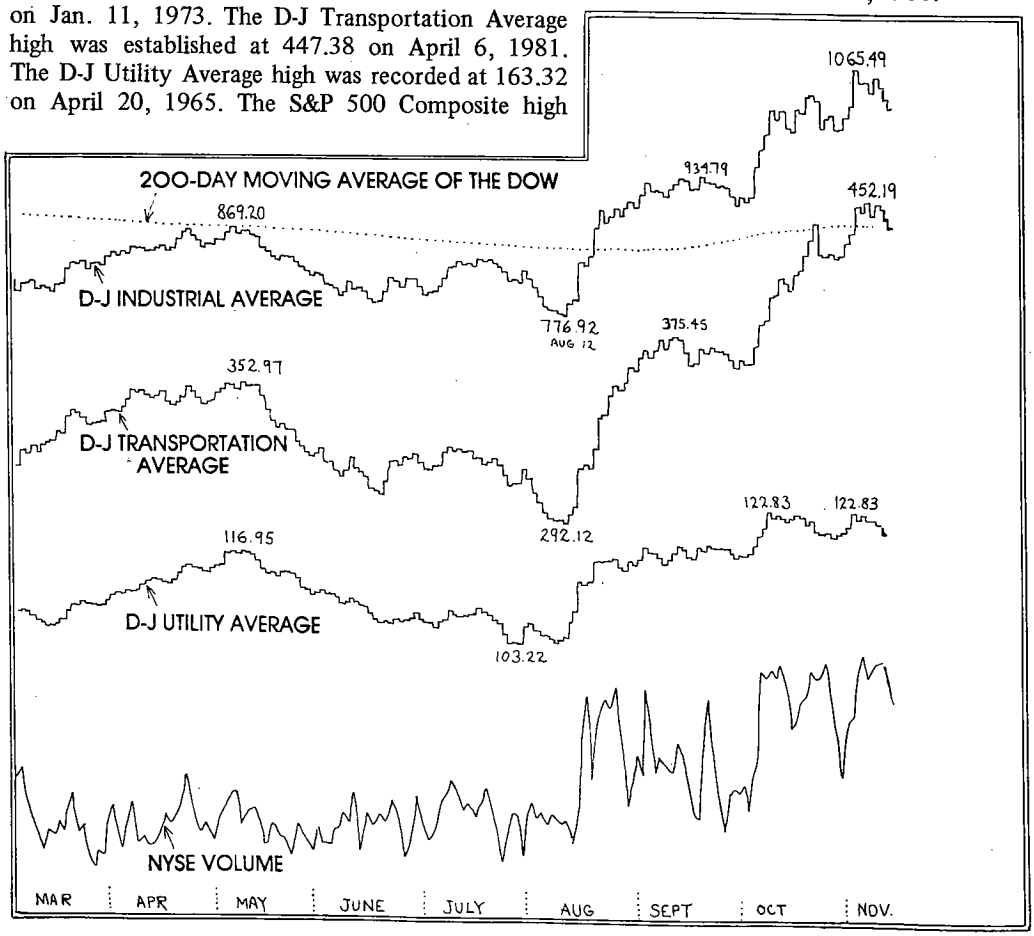
Technically, the rise was fueled by heavy odd-lot selling (3.5 shares sold for every 1 purchased) and a record short interest. Fundamentally, the advance was fueled by a frightened Federal Reserve Board which was gunning the money supply for all it was worth (since late-August the M-1 money supply has risen at a 18% rate!). Furthermore, gloomy unemployment figures have only served to spur the Fed to boom the money supply and lower the discount rate (five cuts in the rate since July).

The net result has been a mind-boggling stampede of foreign and institutional money out of cash and liquid investments and into stocks. Since August 12 it's been a case of all buyers and no sellers – to the tune of the greatest volume explosion in Wall Street history.

From an historical standpoint, the following should be noted. The previous D-J Industrial all-time high was recorded at 1051.70 on Jan. 11, 1973. The D-J Transportation Average high was established at 447.38 on April 6, 1981. The D-J Utility Average high was recorded at 163.32 on April 20, 1965. The S&P 500 Composite high was recorded at 140.52 on November 28, 1980. The NYSE Composite high was hit at 81.02 on November 28, 1980, the Value Line Composite high was touched at 188.64 on December 13, 1968.

FRONT PAGE COMMENT: Any way you look at it, the November election results are going to make it harder for President Reagan to continue with his favorite programs. The election results in the Senate were a standoff. But in the House the count has changed dramatically. Up to November, Reagan was able to draw on a pool of 192 Republicans and 77 conservative Democrats. The new Congress will give him a pool of only 165 Republicans and 77-80 "helpful" Democrats. And in the Republican political base as represented by the Governorships, the result was a fiasco. Republicans won 27 of the 36 Governor races, giving the Dems all but 12 of the states in the nation.

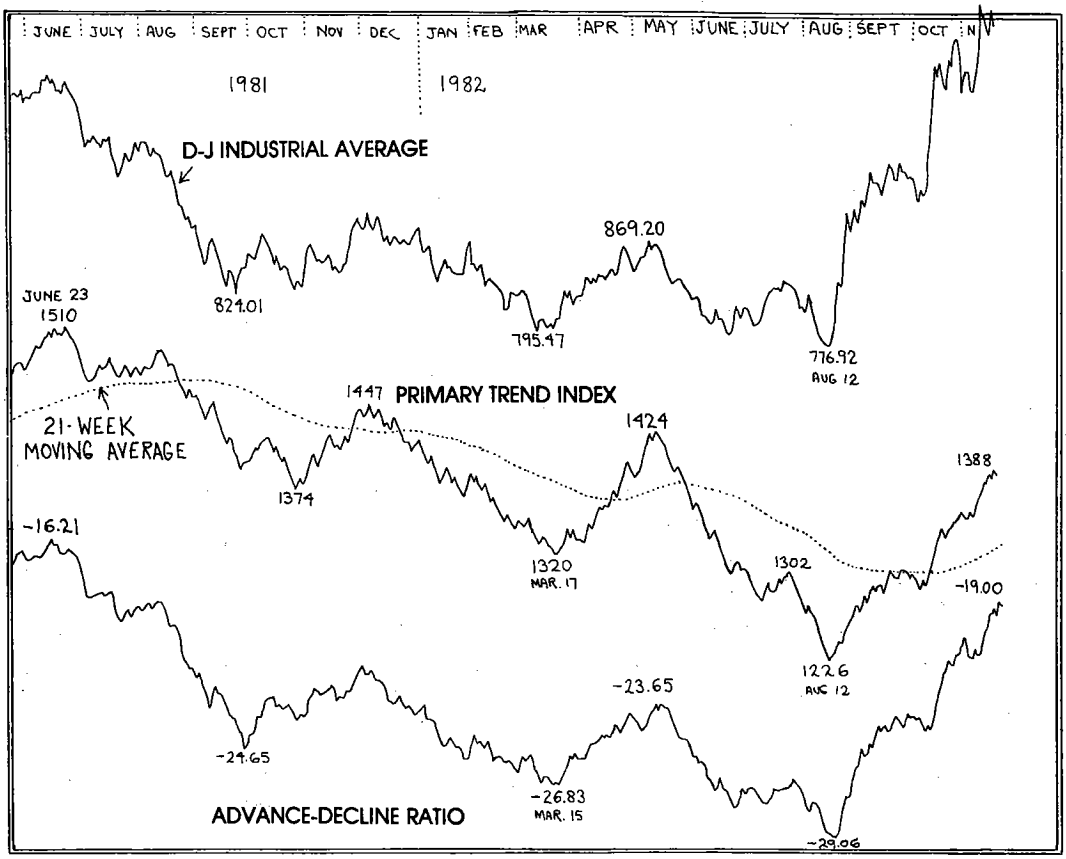
The first results will be as follows: (1) The MX missle program will never get off the ground. (2) There will be heavy resistance to further nuclear buildup, and the defense budget will be under pressure. (3) There will be extreme pressure to spend more on social programs. (4) Cuts of any kind in Social Security will be difficult to come by. (5) The annual Federal deficit will continue to head skyward – towards $200 million. (6) Taxes will also be headed higher – particularly corporate taxes.



On November 3, 1982 the D-J Industrial and Transport Averages rose to new highs, along with the S & P 500, and the NYSE Composite. The Value Line Composite and the D-J Utility Average failed to make new highs.

Now the question: is it conceivable that the D-J Industrials and Transports (confirmed by the S & P 500 and the NYSE Composite) can go to record highs without this being a primary bull market? On the face of it, I would have to say no, that the breakout by the major Averages imply that the primary trend of the market has been up since August 12, 1982. But in all honesty I must also say that I am uncomfortable with this market. The explosive action on Wall Street since mid-August is without precedent.

No market in history has risen from a bear market low to a record high without a full correction. No market has ever traded billions of shares in a period of a few months. No bull



market has ever started with a Time magazine cover advertising the event in advance. Last week a veteran market observer called me and said, "Russell, I'll be honest with you. I've been watching market action for thirty years – and I don't know whether we're seeing the beginning or the end on Wall Street."

Question: Russell, this market has been going up ever since August 12. Do you concede that this is a primary bull market?

Answer: The market can do anything, and the events of the past three months prove it. This is one of the few times in history when the major averages have broken out to new all-time highs without the Dow Theory ever giving a bull signal. But it happened, and there isn't anything I can do about it.

These are unusual times and I said, the stock market can do anything. On the face of it, the new highs in the major averages should serve to signal that the primary trend of the market is bullish. But I still have nagging doubts about the picture, and one of the things that bothers me is the *widespread acceptance of the bull story* on Wall Street and in magazines and newspapers everywhere. I'm used to primary bull markets that develop amid skepticism, disapproval and denial. But perhaps the level of investor sophistication has now risen to such an extent that the bull can be identified just weeks after he has taken command.

Question: What do you make of the record volume that has accompanied the rise?

Answer: This is another extraordinary phenomenon. Nothing attracts headlines as surely as record volume on the NYSE. And since most bull markets start on very low volume – with very low profiles, this extraordinary rise on headline-catching volume is all the more atypical. A great deal of the volume came from two sources: (1) institutions who are part of the great "performance" race. These institutions rushed into the market as it rose, buying incredible amounts of stock even while the Dow was better than 200 points above its August lows. (2) Foreigners worried about their own economies, their currencies and the inroads of socialism, also poured money into the US market. Their buying along with buying of institutions produced record volume day after day.

Question: Russell, what odds do you give for a correction in this area?

Answer: Every move (whether primary, secondary or minor) in stock market history has been subject to correction. The only question is that of timing. Usually, the longer a correction is held off, the more important the correction is when it finally arrives. It is axiomatic that corrections come when they are least expected and when they are least wanted. The higher the current advance goes without a full correction, the more severe the correction will be when it finally arrives.

Question: You discussed the parabolic-curve rise of the Dow in the last Letter. Has anything happened since to alter your thinking on this?

Answer: No, but you will notice (see the stock page of the WSJ) that the Dow has embarked on its third upward spike-rise from the August low. Each consolidation prior to a new rise has been shorter than the last, and the Dow is now in the vertical phase of its parabolic curve. Past history suggests that there is no "soft landing" from this kind of parabolic rise.

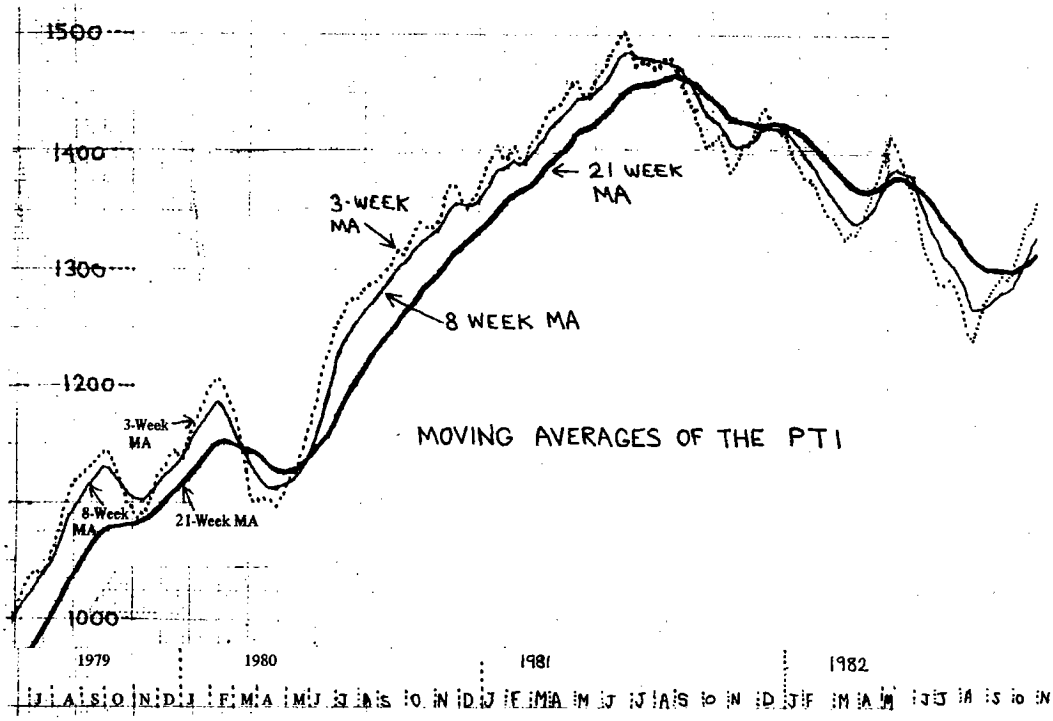
Question: What do you think are the dominant considerations in the market now?

Answer: I feel that the market is heavily over-bought now. For instance, 88% of all NYSE stocks are now above their 30-week moving average. This implies that the market is straining on the upside. The Dow is now 155 points above its 50-week moving average, and this too suggests a very over-heated rise. The put-to-call ratio is now very low, and this means that speculators have given up making money on the put (short) side of the market. Finally, NYSE specialists (who have a good record) have been shorting heavily during October and November. These market-makers get taken once in a while but not too often (and they now need lower prices to get out even).

So the upshot is that if you buy here (even if the Dow runs 50 points higher) you're going to be losing money during the first correction.

Question: What about the Primary Trend Index, what do you see here?

Answer: The PTI bettered its 21-week moving average on October 8. A week later the 21-week MA for the PTI turned



up. This bothered me at the time (from the bear standpoint) and here's why. Note that during the December bear market rise and again during the May rise the PTI climbed temporarily above its 21-week MA. When the PTI climbed above its 21-week MA again in October I felt that this was too strong a performance for the PTI during a bear market. I thought that following the May collapse the PTI should have held BELOW its 21-week MA for a long period of time. So when the PTI climbed above the 21-week MA for the third time in October– that was a bullish indication.

I wondered at the time whether the bear trend could not be at least temporarily ending. There wasn't enough weakness to satisfy the bear position. But I felt from the safety standpoint that I should wait for the appearance of a Dow Theory bull signal. Such a signal (and this is almost unprecedented) never came. It was a most frustrating situation for me. But then, as I have written many times over the past 25 years, "they don't run the market for Richard Russell's benefit."

All of this has made me more determined than ever to give prominent status to my Primary Trend Index. The fact is that I have more and more faith in this Index as the years go by.

Question: What are you watching for on the PTI now?

Answer: I find it extraordinary that the PTI has not yet bettered its May 11 high of 1424. The Dow has bettered its May high, the A-D ratio has bettered its May high; why has the PTI lagged so badly? Only time will tell us. But I feel that it is imperative that the PTI take out the May high.

On the other hand, as long as the PTI holds above its rising 21-week MA the trend of the PTI must be considered as bullish.

Question: What is the PTI telling us from the long term standpoint?

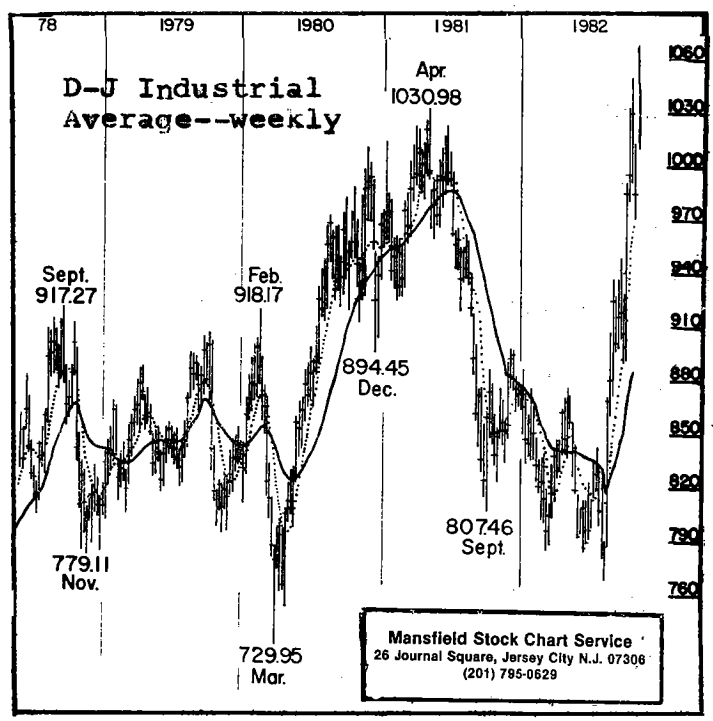
Answer: For this I have included my chart (page 3) of the three moving averages of the PTI, and a little historical perspective is instructive here. Note that the 50-week MA (heavy black line) rose almost without interruption throughout 1979, 1980 and most of 1981. The 50-week MA turned down on the week of September 3, 1981 and continued down to a low of 1301 on October 7, 1982. The 50-week MA of the PTI is now at 1316. Only 15 points above its 1982 low.

Question: So what are you saying?

Answer: Between 1979 and 1981 the 50-week MA rose almost 400 points, and during that time it was profitable to hold common stocks. *The 50-week MA has now just started up.* If we are now in a major bull market as many analysts claim, then the PTI should have a long way to go on the upside. And there should be plenty of time to buy and garner profits. However, in the current over-bought state of the market I think the odds favor *waiting for a correction* – even though the PTI has turned bullish, and even though the 13-week MA of the PTI has now crossed above the 50-week MA.

Question: What are the D-J Averages telling us now?

Answer: The recent record highs were 1065.49 for Industrials, 452.19 for the Transports (see page 1 chart). These highs were made after an extended rise. In fact, the Industrial peak was made with the Dow an unbelievable 182 points above the 200-day moving average. All my studies indicate that despite the record highs of early November, the market is overdue for downside action.



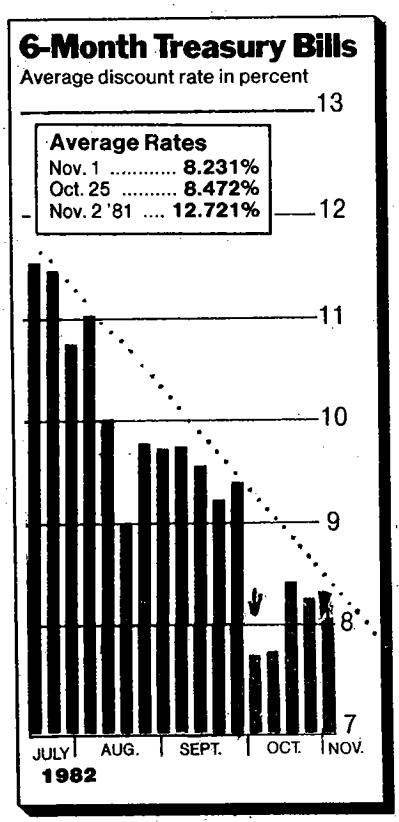
Question: You've mentioned the long-term moving average of the Dow repeatedly. What signifigance does it have now?

Answer: The accompanying chart (weekly Dow) shows the action since mid-1978. Note the huge parabolic spike of 1982. This spike has taken the Dow far above the 30-week moving average (solid black line) depicted on this chart. I know of no instance in market history when, following a sharp upward spike, the Dow did not come down and break at least temporarily BELOW the 30-week (or the 200-day) moving average. The 30-week MA is about 885 now and rising rapidly. The test of strength for the Dow is now underway.

INVESTMENT POSITION: In view of the new highs in the D-J Industrials and Transports, and in view of the bullish trend in the PTI, I feel that the stock market deserves the designation of "primary bull." I have wrestled with this in my own mind, and I must say that I still harbor reservations. But I won't fight my own indicators, and as I pointed out in a previous section, the 50-week moving average of the PTI is just pushing off its base. If we're dealing with a true primary bull market then 300-500 upside points on the PTI would not be extraordinary.

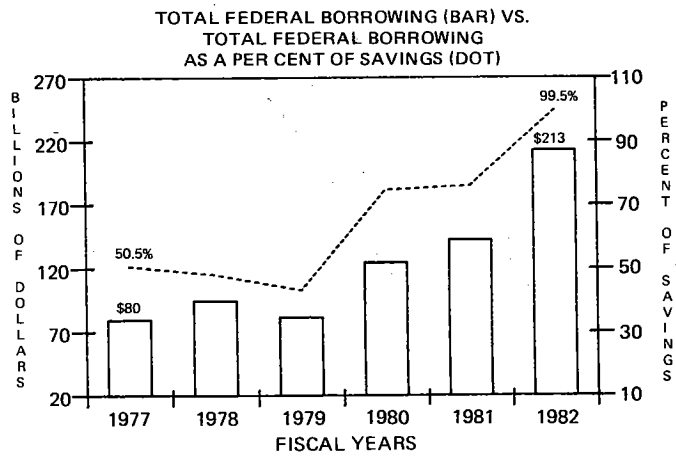
I continue to feel, however, that prudence indicates buying stocks on the FIRST FULL CORRECTION in the bull market. We have not had anything that resembled a full correction so far. Corrections begin when it appears "impossible that the market can turn down." Of late, the market has had the look of invincibility.

MONEY RATES: The most widely-held conviction, the most popular forecast today, is that interest rates are headed lower throughout the rest of 1982 and into 1983. If this prediction comes true, it will be the most incredible "mass-consensus forecast" in Wall Street history.



As you can see from this chart of 6-month T-bills, interest rates hit their low during the first week of October, 1982, and they have not been lower since. They may go lower, they may collapse as predicted by so many financial analysts and economists, but it is impressive to me that with the Fed doing everything it can to bring down rates, the rates have not dropped anywhere near as low as they were during the last recession. And if the 6-month bills hit 8.5% over the next few weeks, they will have reversed the downtrend.

Why? Why are rates not collapsing? One reason (stop me if you've read this before these reports) is that our Government is producing some unbelievable deficits. As things stand, the on-budget deficit for 1983 will be about $175 billion with another $20 billion for off-budget. That's a nice little package of money to raise. In fact, according to this chart (from Manufacturers Hanover) the Government needs in 1983 will sop up roughly 100% of all savings for the year. To put it mildly, I feel there are going to be a lot of shocks in the money market during 1983 – 1984 and '85.



NOTES & QUOTES: You think you're paying a lot for taxes. You are! But harried taxpayers in other countries pay more. Here's a run down on what you'd keep if you make $20,000, $50,000 and $100,000 and are married with two childred. Note the huge take by European governments. But the trouble is now starting. The WSJ (Nov. 11) notes "Generosity's Price: Europe's slump swells social security cost, and the ax begins to fall. Countries are now trimming benefits as the depression cuts the government's tax take." So it all boils down to this – the government can only give to the people what it takes away from them, in the form of taxes or loss of buying power through inflation.

Take-Home Pay

Take-home pay in three income brackets after federal taxes and social security*

	$20,000	$50,000	$100,000
Switzerland	$17,400	$37,000	$63,000
France	$16,600	$37,000	$64,000*
Luxembourg	$16,200	$36,500	$53,000
United States	$16,200	$35,500	$63,000
Spain	$15,600	$36,500	$62,000
Greece	$15,000	$29,000	$49,000
Ireland	$13,800	$26,500	$46,000
Italy	$14,200	$32,500	$58,000
Norway	$14,000	$24,000	$39,000
West Germany	$13,800	$30,500	$52,000
Belgium	$13,400	$26,500	$42,000
Finland	$13,400	$24,500	$40,000
United Kingdom	$13,400	$29,500	$50,000
Netherlands	$13,000	$26,000	$41,000
Austria	$12,800	$26,000	$46,000
Portugal	$12,600	$21,000	$31,000
Denmark	$12,200	$21,500	$37,000
Sweden	$11,600	$17,000	$24,000

*For married couple with two children

* *

With the election over, the fellows around the President got together to kick the whole picture around. According to an informant to Associated Press, these are some of the things that occurred:

> **But Mr. Reagan sat mostly silent at the polished table in the Cabinet Room, asking occasional questions and trying to look on the brighter side, as he listened to the litany of troubles ahead.**
>
> **Martin Feldstein, the new chairman of the President's Council of Economic Advisers, opened the Tuesday meeting with the economic overview. He predicted an eventual recovery from the recession but added that it would be weak and slow in coming, and that unemployment would remain high for the next several years.**

Budget Director David Stockman, carefully clinical, followed up with forecasts that the weak recovery and continued high spending would mean that budget deficits for this fiscal year and the next will range from $175 billion to $200 billion with no decline in sight.

Richard S. Williamson, the President's assistant for intergovernmental affairs, reported that cuts in federal aid and the long recession had left most of the states and many cities near financial exhaustion.

And on Wednesday, after the Republicans had been beaten at the polls, White House congressional lobbyist Martin Duberstein said the President could no longer count on a "conservative coalition" on Capitol Hill.

Against the background of the recession, climbing deficits and the sinking Republican political fortunes, leaders of both parties have urged Mr. Reagan to change course on his tax and budget cuts and his proposals for increased military spending.

But the President, despite his advisers' gloomy forecasts, made no new moves. Nor was he expected to.

* *

For 20 years people have asked me why I live in La Jolla (which is actually a suburb of San Diego). For 20 years I've been telling people that San Diego is the finest place to live in the nation. When I arrived here in 1961 there were two huge drawbacks. First, I couldn't get the WSJ in the morning (it had to be mailed out to the Coast). Second, I couldn't get the NY Times. Now both of these great newspapers are printed in California each day (via satellite) and delivered to my door around 4 A.M. So within an hour I can be in the desert, be at the seashore, be in the Laguna mountains, be in Mexico, be on a tennis or golf course or be in downtown San Diego. Or I can stay home and read the NY Times.

Evidently, the news has seeped out over the last 20 years, and I no longer get that question, "What are you doing out in Sandy Yeggo?" Here's a rundown by the Chicago firm of Heidrick and Struggles, Inc. on the desirability of 18 major US cities. The quiz was sent to 790 corporate executives of vice-president status or above. The primary considerations were (1) climate, (2) culture, (3) recreational facilities, (4) cost of living.

	Overall Rating	*Eager to go to*	*Won't go to*
San Diego	3.02	27.6%	5.6%
San Francisco	3.02	25.1	4.8
Phoenix	2.56	8.6	12.5
Dallas	2.51	7.9	12.9
Washington, D.C.	2.45	7.2	15.3
Los Angeles	2.29	5.8	18.6
Chicago	2.25	3.0	16.6
San Antonio	2.23	4.3	22.0
Philadelphia	2.20	2.7	21.9
Houston	2.19	2.9	21.1
New York	2.08	6.0	26.6
Baltimore	2.00	1.4	29.2
Memphis	1.99	1.2	30.2
Milwaukee	1.89	.7	32.7
Columbus	1.88	1.4	37.1
Indianapolis	1.85	.1	36.0
Cleveland	1.70	.4	43.6
Detroit	1.56	.5	50.9

SOURCE: Heidrick and Struggles

* *

From our "Sad State of the States" Dept. Don't think your Federal Government is the only one practicing fiscal insanity. Now it turns out that California will run a $1.1 billion deficit for the current fiscal year. In the meantime, New York State will have to borrow $350 million to pay its bills over the next two months. The Empire State has just seen its rating dropped to its lowest level (by Standard & Poor's) down to A plus from AA plus. NY thus joins Pennsylvania and Michigan at the bottom rung of the state rating ladder.

* *

GRANVILLE INDICATOR? Back in January, 1981 when Granville gave his famous bear signal he was widely pooh-poohed by Wall Street. By August, 1982, people realized that Joe was right. But then Joe missed the turn (like yours truly) and had his people ride the great rally in a fully short position. But here comes the Wall Street Journal (Nov. 12) putting Joe down and making fun of him. When they feel confident enough to make fun of Granville in a national newspaper, I wonder if the market isn't near trouble. Thought: when EVERYONE follows and believes a name analyst – watch out. When NOBODY believes the same analyst – watch out again.

* *

Nobody hates smoking cigarettes like an ex-smoker. I used to smoke 2.5 packs a day (I quit 12 years ago, and quitting was the best thing I ever did). How did I quit? Fear, I sensed I was killing myself, so after 25 years of smoking I quit cold. Four days later I had a heart attack. I've never smoked again, and I've never had trouble with my heart again. A connection– I believe so.

This piece from a letter (from a medical scientist) to the NY Times stopped me cold. I want to repeat it here. I think it makes a good case for getting off the smoking habit. If it scares you, take that as a plus. The best way to get off cigarettes is through fear. Intelligent, logical people get off tobacco.

> **Two radioactive isotopes, polonium-210 and lead-210, are highly concentrated in particles in cigarette smoke. The major source of polonium is the phosphate fertilizer used in growing tobacco. In a person smoking one and one-half packs of cigarettes per day, the annual radiation dose is equivalent to that of 300 X-ray films of the chest.**

* *

If you live in the Eastern US and you want to thaw out, you fly down to Florida. In the West, the place for sun and fun (assuming it isn't raining there) is Hawaii. I've been hearing about the wonders of Hawaii for all the 21 years that I've been out here. So I've decided, as they say in modern parlance, to "do Hawaii." Paula and I are taking the whirlwind stock market letter writer's trip to the islands.

It will only be a five-day trip, but that's a long time if you're dealing with Wall Street. At any rate, by the time you receive this report I should be back, tanned, rested, and ready anew to do battle with the stock exchanges of the world.

* *

Remember the cry for "The reindustrialization of America" that emerged only a year ago. Well, the cry was OK, but things didn't work out that way. In fact, what has actually been going on is termed "deindustrialization. This clip from the Nov. 2 Christian Science Monitor tells the story.

Whether President Reagan or somebody else sits in the White House, they maintain, is almost incidental; what they fear is that business-as-usual isn't going to come back to America without prodding.

There is general agreement on the problem:

• There is 10.1 percent unemployment and 12 million unemployed, a number which seems to be going higher.

• Corporate stagnation means only about 68 percent of factory capacity is being used.

• Low productivity and expensive relief programs keep the deficit at unprecedented heights.

• Stimulus to the economy by cutting taxes has been of doubtful value.

• And since mid-1960, American factories have migrated abroad, sending back lower-cost goods made by less expensive foreign labor and threatening a worldwide trade war.

Economic crises produce new schools of thought: John Maynard Keynes came 50 years ago; more recently the country sharply debated "supply-side economics."

Now the challenge is identified as "deindustrialization," meaning that big US industries have been moving from home factories to cheap labor abroad and that the structure of American industry is in flux. The new philosophy is set forth by Bennett Harrison of MIT and Barry Bluestone of Boston College in their book, "The Deindustrialization of America; Plant Closings, Community Abandonment, and the Dismantling of Basic Industries."

* *

GOLD: With M-1 rising at a rate of almost 16%, the money supply can be said to be exploding. But according to the latest report by US purchasing agents, the economy in October was no better than it was in September. What's it going to take to "float" this slumping economy out of recession? My guess is that it will take M-1 expansion of near 30%. Would the Fed dare try this kind of monetary expansion (inflation)? I doubt it, but who knows. After all, we have a big Democrat majority in the House, we have a big Demo majority in the state Governorships; if unemployment continues to climb, who knows what the Fed may be tempted to try.

As I've said many times before, "not enough inflation in today's debt-ridden economy – is deflationary." The rising tide of debts is basically deflationary. The creation of credit to carry those debts is basically inflationary. And that's where the inflation-deflation battle lines are drawn. So far, deflation is winning. But there will be increasing pressure on the Fed and the Administration to inflate.

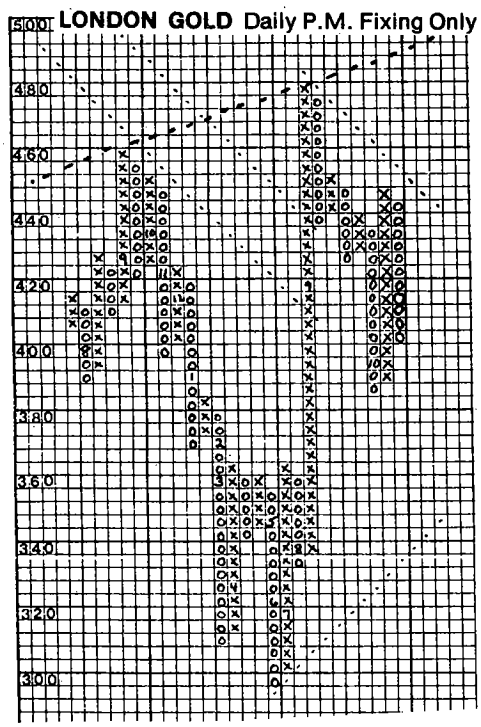
All this gold understands. Gold bulls are betting that the Government will do what it always does when business slumps – inflate. Gold bears are betting that the Administration and the Fed don't have the chutzpah to inflate to the point where today's recession-depression can be turned around. Meanwhile, the higher the debts (and they are going higher) the more credit creation it will take to keep the economy going. The shark is finally eating its own tail.

I have an awful lot of subscribers who are gold bulls. They own gold, and they want the price of gold to go up. Personally, I'd like to see gold hold in the 400-450 area. I'd like to see gold simmer down and sit – for the good of the country. If gold breaks out above 510 it's going to be a signal that inflation is taking hold. And if gold breaks below 380, below its 50-week moving average, that will be a deflationary red flag. A break to 380 will tell us that the nation's debt is eating us up alive – and that is deflationary.

I would take a bearish view of sliding gold here. I would view it as a sign that the debts are swamping US industry and government and that we are heading into even harder economic times. Remember, the Fed has been trying to "gently inflate" this nation so that corporations and government may remain solvent. But gentle inflation may not be enough in the face of a skyscraper of debts. Gentle inflation, in fact, may sink this country into a deflationary depression. I feel that the price of gold will be a key indicator of where we're going from here on.

The primary or 50-week moving average of gold is now 393. The 13-week MA is 410. The 5-week MA is 416. Gold is showing weakness in that the spot price is below both the 5 and 13-week MAs.

This P & F chart of gold shows the nearer term picture. A spot price of 452 would be needed for a new bullish signal. On the other hand, a price of 380 would be bearish, rupturing the whole recent structure. If gold is in a bull market then the potential head-and-shoulders pattern shown in the chart should hold. The price would have to go above the 480-500 level for a major breakout of this huge potential base. (chart courtesy of Chartcraft, Larchmont, NY).



NEXT MAILING: December 1